HJ
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HIGGS & JOHNSON
Counsel & Attorneys-at-Law

BULLETIN

FATCA AS IT RELATES TO BAHAMIAN LAW

Overview of FATCA

In 2010, the U.S. government enacted the *Hiring Incentives to Restore Employment Act* (the "*Act*"). The *Act*'s principal purpose is to provide U.S. employers with the necessary incentives to hire and retain new employees. With exemptions and tax credits offered by the *Act*, the U.S. Government has chosen to offset its costs by incorporating the provisions of the *Foreign Tax Account Compliance Act of 2009* ("*FATCA*"). *FATCA* implements measures which challenge the concept of offshore financial privacy, by measures such as increased reporting requirements and taxation of foreign institutions. By *FATCA*, the Internal Revenue Service (the "*IRS*") may impose additional reporting requirements for U.S. persons who hold offshore financial accounts or enjoy offshore financial services. These reporting requirements are in addition to the current foreign banking reporting requirements and require disclosure of a broader class of foreign assets.

Reporting Requirements of FATCA

Under the provisions of the Act, any U.S. person who holds an interest in any foreign financial assets must disclose the extent of such assets by attaching a disclosure statement to his or her annual income tax return, so long as the aggregate value of all foreign financial assets exceeds fifty thousand dollars. Pursuant to the Act, foreign assets include foreign financial accounts, foreign stocks and securities, and interests in foreign entities. Moreover, all U.S. entities "formed or availed of for purposes of holding, directly or indirectly, specified foreign financial assets," will be subject to the same reporting requirement.

Importantly, beginning in 2014, the Act will mandate that all foreign financial institutions enter into an agreement with the U.S. Treasury Department to report information about its U.S. account holders each year. A "foreign financial institution" is defined broadly to include any foreign entity that (i) accepts deposits in the ordinary course of a banking or similar business, (ii) holds financial assets for the account of others as a substantial portion of its business, or (iii) is engaged (or holds itself out as being engaged) primarily in the business of investing, reinvesting or trading in financial assets (including securities, partnership interests, commodities, or any interest in such securities, partnership interests or commodities). Accordingly, this broad definition encompasses foreign investment banks, foreign commercial banks, foreign insurance companies, foreign hedge funds, foreign private equity funds, and foreign securitization vehicles.

Higgs & Johnson
Ocean Centre
Montagu Foreshore
East Bay Street
P O Box N 3247
Nassau, BAHAMAS
Tel: 242 502 5200
Fax: 242 502 5250
E-mail: info@higgsjohnson.com
Web: www.higgsjohnson.com

Foreign financial institutions will be required to determine which of their equity and debt holders (and certain other of their counterparties and other "account holders") are U.S. account holders, and to report this information to the IRS or otherwise be subject to a 30% withholding tax on the foreign financial institution's U.S. source income and/or the proceeds of certain sales and other dispositions.

Prior to the year 2016, foreign financial institutions will be required to report the name, address, and taxpayer identification number of each account holder who is a U.S. taxpayer individual and where it is a U.S. taxpayer entity, the name, address and taxpayer identification number of each substantial U.S. owner; and the account number. Beginning in 2016, the required reporting will be expanded to include income from U.S. accounts, and beginning in 2017, full *FATCA* reporting with respect to U.S. accounts will be required.

If the foreign financial institution is unable to obtain information from a specified account holder, it may either (i) withhold the 30% withholding from the payments it makes to the recalcitrant account holder, or (ii) elect to receive its U.S. source payments, subject to 30% withholding on the portion that is allocable to the recalcitrant account holder.

Further, if an account holder fails to provide the requisite information, a 30% withholding tax will be imposed on all withholdable payments made to foreign financial institutions. For such purposes, withholdable payments are defined as (1) any gross proceeds from the sale or other disposition of any property of the type which can produce interest or dividends from sources within the U.S., and (2) any U.S. source payment of interest (including original issue discount and portfolio interest), dividends, rents, salaries, wages, premiums, annuities, compensation, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits and income, if such payment is from sources within the U.S.

FATCA and Current Bahamian Law

The implementation of reporting requirements under FATCA presents certain challenges which will require consideration and satisfactory resolution.

Banks and Trusts Companies Regulation Act

The *Banks & Trusts Companies Regulation Act, 2000* (the "*BTCRA*") imposes a duty of confidentiality on all licensees of the Central Bank of The Bahamas ("*licensee*"). Section 19 of the *BTCRA* expressly provides that no person acquiring information in their capacity as a director, officer, employee or agent of a financial institution shall without the express or implied consent of the customer concerned, disclose to any person any information relating to the identity, assets, liabilities, transactions or accounts of a customer. There are very limited exceptions to this confidentiality provision.

Data Protection Act

Further, under the *Data Protection (Privacy of Personal Information) Act, 2003*, (the "*DPA*") restrictions are put in place to safeguard and protect personal information of living individuals. By section 6 of the *DPA*, a data controller may not use or disclose personal data in any manner incompatible with the purposes for which it is kept. Additionally, the DPA requires that appropriate security measures shall be taken against unauthorised access to or alteration, disclosure or destruction of the data and against accidental loss or destruction.

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Confidentiality Under the Common Law

The duty of confidentiality imposed on a financial institution in respect of its customer's affairs is imposed on a financial institution not only by statute but also by the common law. In the leading case of *Tournier v. National provincial and Union Bank of England (1924) 1 KB 461*, which defined the scope of a bank's duty of secrecy, the court held that a bank had a duty of secrecy to its customer with regard to its customer's affairs, subject to certain qualifications:

- where disclosure is under compulsion of law;
- where there is a duty to the public to disclose;
- where the interests of the bank require disclosure; and
- where the disclosure is made by the express or implied consent of the customer.

Reconciling FATCA with Bahamian Law

Financial institutions must give attention to strategies which resolve the issues raised by reporting requirements of *FATCA* vis a vis the statutory and common law duty of confidentiality which is owed by a financial institution to its customers. In certain cases, resolution may be achieved by simple written waiver by customers of their rights under Bahamian confidentiality and privacy laws which would allow foreign financial institution to report relevant information pertaining to its customers to U.S. tax authorities. It is anticipated that prudent financial institutions will continue to consult in earnest with their attorneys to ensure that all regulatory and statutory requirements are satisfied and that clients' interests are served in the context of evolving regulation.